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BEFORE THE

HOUSE COMMITTEE ON GOVERNMENT REFORM
SUBCOMMITTEE ON GOVERNMENT MANAGEMENT, FINANCE AND ACCOUNTABILITY

ON THE
OMB'S FINANCIAL MANAGEMENT LINES OF BUSINESS INITIATIVE

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Introduction

Mr. Chairman and members of the subcommittee, thank you for allowing AFGE, which represents more than 600,000 federal employees across the nation and around the world, this opportunity to present our views on the Office of Management and Budget's (OMB) controversial Financial Management Lines of Business (FMLoB) initiative.

Mr. Chairman, AFGE commends you in particular for your attention to the details and consequences of the initiative, your determination to get answers about the initiative from a frequently unforthcoming OMB, and your interest in hearing a diverse range of views on the initiative at today's hearing.

We started hearing about the initiative in late 2005 in the form of warnings from senior procurement officials with whom we normally spar over the OMB Circular A-76. Official after official, in agency after agency, warned us that an alternative to the A-76 circular was being prepared in relative secret, and that this alternative to the A-76 circular would be used to perpetrate "direct conversions" of information technology functions. "Direct conversions" is a polite euphemism for taking work away from federal employees and giving it to contractors without any public-private competition or proof of savings, i.e., stealing dollars from taxpayers and stealing jobs from federal employees. And those warnings have proven to be accurate. The OMB insists that the A-76 circular will be used in the FMLoB initiative. But in fact, the OMB's guidance

1. encourages agencies to give work to contractors without any public-private competition;

2. fails to ensure that related work transferred to a federal shared service center that is ultimately contracted out is not first subject to public-private competition;

3. allows agencies to use a version of the subjective "best value" (sic) competition process so extreme and so vulnerable to abuse that it has been outlawed by the Congress and repudiated by the OMB;

4. encourages agencies to make up their own rules for specific competitions; and

5. fails to ensure that related work that's already been outsourced will be reviewed for insourcing.

OMB's Edict: The Fundamentally Flawed FMLoB Initiative

The FMLoB initiative is typical of the schemes that come out of the OMB, regardless of who is president, in which OMB officials insist on substituting their own judgment for that of the career officials in agencies who are actually responsible for the delivery of important services to the American people and who are the most knowledgeable about what is necessary to ensure that such services are actually provided.

In requiring that all agencies, in all but the most extraordinary circumstances, dismantle their financial management functions in favor of having such vital services instead be provided by a tiny handful of contractors and agencies, the FMLoB initiative also reflects the OMB's quintessential bigger-is-better, one-size-fits-all approach. That each agency has its own mission, its own workforce, its own culture, and, most importantly, its own needs for accountability and quality control, all of that is imperiously swept aside by OMB officials who insist that they know best.

In fact, OMB officials should restrict their role to setting standards and metrics for the performance of financial management services—and then getting out of the way so that agency managers can make their own decisions as to what arrangements would best promote their missions and minimize their costs. Current funding shortfalls and budget crunches are all the incentives agencies need to generate efficiencies in the performance of financial management services. Divestiture-and-consolidation/privatization, along the lines of the FMLoB initiative, may be an appropriate option in some instances; however, it should not be dictated by the OMB in all but the most extraordinary circumstances.

While FMLoB certainly qualifies as a classic OMB power-play undertaken at the expense of agencies' autonomy, the integrity of the initiative is further undermined by this OMB's obsession with wholesale privatization. As one contractor insisted in a discussion earlier this year about another lines of business initiative, "The government shouldn't really be in the HR/payroll business."[1] In weaker moments before contractor gatherings, OMB officials have let similar feelings show: "`We want improved focus on agency core missions,' (said OMB's associate administrator of E-government and IT). Agencies should spend `more time and resources fulfilling their own responsibilities.'"[2] That has often been this OMB's code for forcing agencies to divest themselves of support services and to directly convert them to contractor performance.[3] Although this OMB's officials consider themselves to be on the cutting edge, their wholesale privatization approach is rejected by the less ideologically blinkered managers in the private sector and local government.[4]

This OMB is also well-known for its hubris and overreach on issues affecting federal employees. Its schemes to undermine civil service protections against politics and favoritism and to bust federal employee unions in the Departments of Defense and Homeland Security have been struck down by the courts. Its National Security Personnel System (NSPS) is so disliked that not a single member of the House of Representatives was willing to speak on the floor in opposition to an amendment to block funding for the labor relations and employee appeals portions of the NSPS regulations that was offered last week to the FY2007 Defense Appropriations Bill. And, of course, the Congress rarely passes up opportunities to reject and reform this OMB's scheme to force agencies to review for privatization 850,000 federal employees through "competitive (sic) sourcing", blustery veto threats notwithstanding. Indeed, as the Congress, particularly the Appropriations Committees, looks more closely at the FMLoB initiative, the more likely it is to meet a similar fate.

OMB's Guidance on "Competition" (sic) for the FMLoB Initiative

OMB officials have always known what *they* wanted for the FMLoB initiative, and they haven't been particularly interested in what the Congress or any of the stakeholders have to say. As Clay Johnson, OMB's deputy director for management famously said, "We have said this is the way that we're going to run the federal government and that's the way we're going to run it."[5] And in no aspect of the FMLoB initiative is that more true than with respect to competition. In fact, the OMB published its draft guidance with this stern warning: At this time, the OMB is "soliciting comments on the Guidance from the public. Reviewers are encouraged to comment freely on all aspects of the Guidance, with the exception of the *Competition Framework for Financial Management Lines of Business*…"[6] Indeed, the OMB's FMLoB "competition" (sic) guidance is likely to be in violation of the Administrative Procedures Act for making broad and sweeping changes to the A-76 circular without first providing for a notice and comment process through the *Federal Register*.

AFGE thanks you, Mr. Chairman, for giving the federal employees we represent the opportunity "to comment freely" on the "competition" (sic) guidance that the Administration has otherwise refused to afford to the public, except for a handful of favored contractors.[7]

1. The OMB's guidance encourages agencies to give work to contractors without any public-private competition.

In direct contravention of the A-76 circular, as revised by this OMB on May 29, 2003, the guidance provides that an "agency may, but is not required to follow Circular A-76…for activities involving 10 or fewer FTE's (Full-Time Equivalents)." Please note that the OMB did not thus authorize "direct conversions" in *particular* instances for the FMLoB initiative for financial management functions performed by up to ten FTE's; rather, the OMB is authorizing it in *every* instance

The sanctioning of the abusive "direct conversion" practice is nothing less than a complete change of the OMB's own regulation and policy. Indeed, for almost three years, the OMB has explicitly prohibited the abusive practice of "direct conversions". In 2003, the OMB eliminated "direct conversions" in order to "(c)lose the loopholes that diminish return on taxpayer investment…"[8] At the time, the OMB noted that through "direct conversions," agencies "may be foregoing opportunities to reap savings and make better economic decisions through public-private competition…"[9]

Now, for financial management services, agencies are free to choose providers without any public-private competitions and without any consideration of in-house workforces. Even if an in-house workforce is cheaper and better, the guidance allows an agency "not (to) consider an incumbent provider"[10] if the function is provided by up to ten FTE's.

But wait—it gets worse. Although the "direct conversion" authority nominally applies to all financial management functions performed by up to ten FTE's, in fact, it could be used to contract out far larger functions. According to the Bush Administration's first Administrator for the Office of Federal Procurement Policy (OFPP), agencies had historically broken up larger functions into smaller parts in order to perpetrate "direct conversions"—which played a significant part in the OMB's 2003 decision to eliminate the practice entirely.[11] In other words, the OMB's FMLoB guidance, effectively, allows agencies to steal money from taxpayers and jobs from federal employees on a significant scale through the use of a "direct conversion" practice that OMB officials have already acknowledged is both wasteful and vulnerable to abuse.

2. The OMB's guidance fails to ensure that related work transferred to a federal shared service center that is ultimately contracted out is not first subject to public-private competition.

Much work that is performed by one agency for the benefit of another agency is ultimately performed by a contractor. That is true with respect to agencies that are designated federal service centers pursuant to the FMLoB initiative. The guidance does not ensure that there would be a public-private competition before work is moved to a federal service center that would ultimately be performed by a contractor.

3. The OMB's guidance allows agencies to use a version of the subjective "best value" (sic) process so extreme and so vulnerable to abuse that it has been outlawed by the Congress and repudiated by the OMB.

The use of "best value" (sic) in public-private competitions has been outlawed for the Department of Defense since the enactment of the FY2004 Defense Appropriations Bill and for all other agencies except the Transportation Security Administration since the enactment of the FY2006 Transportation-Treasury-HUD Appropriations Bill. Despite the OMB's blithe assurances, the Congress has understood that the highly subjective "best value" (sic) process is too easily abused to the disadvantage of federal employees and taxpayers, particularly when the OMB is pressuring agencies to privatize functions performed by federal employees whenever and however possible.

Of course, OMB officials also understand how easily the "best value" (sic) process can be abused. The current A-76 circular, as revised by this OMB, in May 2003, severely limits the use of subjective, non-cost factors in all competitions, including for competitions for functions performed by up to 10 FTE's. Indeed, the current A-76 circular states that "(a)n agency shall not use a (best value) source selection process for activities currently performed by government personnel…" unless several specific procedures are followed, including that "the specific weight given to cost or price shall be at least equal to all other factors combined…"[12] In other words when a "best value" (sic) procurement occurs under the current A-76 circular, an objective factor, cost or price, must be as significant an evaluation factor as all others combined.

In direct contravention of the procedures in the current A-76 circular—which, please recall, was completely revised by this OMB—the FMLoB guidance explicitly allows agencies to use the "procedures in FAR Part 15 if conducting a negotiated acquisition, including: application of the policies in FAR 15.101-1 if performing (best value) tradeoffs…" for financial functions performed by up to 10 FTE's.[13] By referencing FAR 15.101-1, the guidance not only sanctions, but actually encourages the use of subjective factors "to consider award to other than the lowest price offeror."[14]

In other words, OMB officials are not just directing agencies to use a "best value" (sic) process for financial management functions performed by up to ten FTE's (as well as for all larger functions that can be broken up illicitly to qualify) that the Congress has outlawed for all functions performed by more than ten FTE's, but they are also directing agencies to use a form of "best value" (sic) that is so subjective and so extreme that OMB officials would not allow it when they revised the A-76 circular in 2003.

But wait—it gets worse. The guidance makes two references to the *general* use of "best value" (sic), regardless of the size of the in-house workforces, on page two of the memorandum and page one of the attachment:

> "An agency may rely on its in-house core financial management system operations without being designated as an SSC only if the agency demonstrates that its internal operations represent a *best value*…over the life of the investment."
>
> "Migration shall result in the selection of a public or private sector service provider with a demonstrated ability to leverage technology, expertise and other resources to achieve *best value* for the taxpayer."

The message of the OMB's guidance is clear: agencies should use subjective factors to make contracting out awards for financial management functions. One can't help but wonder if the OMB's guidance is a thinly-veiled attempt to overrule the statutory constraints imposed on the use of "best value" (sic) in the Defense and Transportation-Treasury-HUD Appropriations Bills.

4. The OMB's guidance encourages agencies to make up their own rules for specific A-76 circular privatization reviews.

The OMB's guidance explicitly encourages agencies to seek "deviations" from the A-76 circular's rules which govern privatization reviews: "Agencies are encouraged to consult with OMB to discuss the most effective and efficient means for conducting a public-private competition."[15]

Encouraging agencies to come up with their own rules for A-76 circular privatization reviews conducted pursuant to the FMLoB initiative is especially worrisome for taxpayers and federal employees when one remembers that the OMB is also encouraging agencies to make subjective award decisions and to give work to contractors without any public-private competitions. What criteria will OMB use in sanctioning deviations? What transparency, if any, will there be for federal employees and taxpayers with respect to agencies requesting deviations and the OMB granting those deviations?

Of even greater urgency, what deviations will OMB officials foist on agencies? Mr. Chairman, allow me to provide the subcommittee with two examples of deviations carried out by the OMB during the tenure of former OFPP Administrator David Safavian, over the objections of agency managers.

In 2005, the Mint decided in favor of the in-house workforce performing truck maintenance after contractors failed to submit a single bid. However, contrary to the A-76 circular and federal law, Administrator Safavian's OFPP insisted that a second A-76 circular privatization review be conducted.[16]

Also in 2005, a contractor at the Defense Distribution Depot Cherry Point, North Carolina, failed to perform so completely that the contract had to be cancelled and the work brought back in-house. However, Administrator Safavian's OFPP, in granting the deviation requested by the Defense Logistics Agency that allowed the Cherry Point Depot to once again have the work in question be performed by reliable and experienced federal employees, insisted that the installation could only use federal employees on a temporary basis and that those federal employees should under no circumstances be allowed to compete before their work was given to another contractor.[17]

The OMB also does a poor job of ensuring that agencies adhere to the terms of their deviations. For example, in 2003, the OMB granted the Department of the Army a deviation to conduct an A-76 circular privatization review of base operations support services at Walter Reed Army Medical Center using the old circular's rules—provided that the Army make a final decision by September 30, 2004, or cancel it. In fact, this A-76 circular privatization review went on so long—a final decision was not made in favor of the contractor until January 2006—that it was in violation of the Anti-Deficiency Act and will cost so much to carry out that taxpayers will lose anywhere from $5 million to $14 million, according to the Army's estimates. Fortunately, the House of Representatives passed without any objections last week an amendment to the FY2007 Defense Appropriations Bill that would prevent the Army from carrying out this illegal and wasteful privatization review, and the Senate is poised to do the same. However, this waste and disruption could have been avoided if the OMB had simply enforced its own rules and forced the Army to cancel this privatization review for being in violation of the deviation.

5. The OMB's guidance fails to ensure that related work that's already been outsourced will not be reviewed for insourcing.

Despite rhetoric that "competitive (sic) sourcing" is all about generating savings and improving services, only work performed by federal employees is ever subject to public-private competition through the A-76 circular. Although OMB officials acknowledge that the public-private competition process in the A-76 circular can be used for insourcing competitions as well as for outsourcing competitions, countless billions of dollars of new work and already outsourced work are reserved exclusively for contractors. Federal employees are rarely if ever allowed to compete for new work and already outsourced work. Almost all work currently performed by contractors has never been subject to public-private competition. Indeed, as the Government Accountability Office and various Inspectors General have reported, contractors acquire and retain countless numbers of contracts on a sole-source basis or with extremely limited competition. If public-private competitions can generate savings for work performed by federal employees, then, surely, similar savings are possible from allowing federal employees to compete for new work and already outsourced work, especially given that federal employees have won, according to the OMB, 80% of the A-76 circular public-private competitions conducted over the last three years.

However, the FMLoB guidance is typical of the OMB's one-sided "competitive (sic) sourcing" approach: competitions (and conversions) for financial management work performed by federal employees, around-the-clock, but none for financial management work already performed by contractors. In fact, the OMB's guidance actually encourages agencies to request deviations from the A-76 circular in order to subject financial management work performed by federal employees to two competitions, the first public-public and the second public-private.[18] Perhaps encouraging agencies to subject federal employees to two competitions is the OMB's way of making up for not subjecting its contractors to even one public-private competition!

Conclusion

Mr. Chairman, I think we can all stipulate, as the lawyers say, that, regardless of whether one supports the FMLoB initiative, the OMB's guidance in no way provides for the use of "competitive sourcing." In fact, the OMB has repudiated its own rhetoric and its own rules in preparing its FMLoB initiative guidance on "competition" (sic). Direct conversions—stealing money from taxpayers and stealing jobs from federal employees—are encouraged for functions up to ten FTE's and thus inevitable for larger functions. Financial management work performed by federal employees can be moved to another agency and then be ultimately performed by contractors without any public-private competition. Agencies can use a form of "best value" (sic) so subjective and so extreme that even the OMB would not include it in the A-76 circular the OMB revised in 2003. The OMB's guidance encourages agencies to come up with their own rules for A-76 circular privatization reviews, which—if past is prologue—will be contrary to the interests of taxpayers and federal employees. And new work and already outsourced work related to financial management will continue to be contractor monopolies.

But wait—it gets worse. The FMLoB initiative is actually a revival of the very worst principles of the OMB's discredited wholesale privatization agenda. In 2001, the OMB imposed numerical privatization quotas on agencies, insisting that they review for privatization under the A-76 circular at least five percent of the jobs on their Federal Activities Inventory Reform Act inventories in FY02 and another ten percent in FY03, as downpayments on an OMB edict that all agencies combined review for privatization by the end of 2004 at least 425,000 federal employee jobs. Agencies were explicitly encouraged to use "direct conversions" to achieve these infamous numerical privatization quotas.

It's so bizarre and it's so perverse that it's difficult to conceive of today—OMB officials insisting, in a classic, one-size-fits all approach, that all agencies, regardless of their needs or missions, compete under the A-76 circular or directly convert specific numbers of federal employees in all but the most extraordinary circumstances—or face sanctions in the budget process. Fortunately, the Congress outlawed the use of numerical privatization quotas; and in its May 2003 rewrite of the A-76 circular, OMB officials were forced to abolish direct conversions, absent specific authority from the OMB.

As OMB officials reluctantly provide this subcommittee with details of the FMLoB initiative, many federal employees are experiencing a sense of déjà vu. Again, the OMB is insisting that all agencies, in all but the most extraordinary circumstances, must compete under the A-76 circular or directly convert a certain number of jobs—or face sanctions in the budget process. However, instead of that numerical privatization quota being 15% of an agency's entire "commercial" workforce, it is instead 100% of an agency's financial management workforce. Indeed, the FMLoB initiative may actually be worse for agencies in that the OMB has unilaterally determined that financial management functions in all agencies, regardless of those agencies' needs or missions, are "commercial" and that all agencies' financial management functions are appropriate for contractor performance. Agencies, consequently, have no flexibility under these new numerical privatization quotas to instead decide to compete or convert functions which are considered clearly "commercial" in place of financial management functions that managers believe are actually best performed in-house by reliable and experienced federal employees. There they go again, indeed.

Mr. Chairman, thank you for this opportunity to present your subcommittee with AFGE's concerns about the OMB's FMLoB initiative. I would be delighted to respond to questions from you and your colleagues.

[1] *Government Computer News*, "Agencies should embrace private outsourcing of HR services: panel" (March 9, 2006).

[2] Ibid.

[3] For example, See GovExec.com, "Procurement chief weighs changes to job competition rules (January 14, 2005): "The Office of Management and Budget's recently confirmed federal procurement chief is rethinking his predecessor's decision to bar agencies from outsourcing even small numbers of jobs without giving in-house employees a chance to defend the positions. Transfers of work to the private sector without a public-private competition, known as `direct conversions,' may be appropriate if an agency decides a certain `business line' is not central to its mission, said David Safavian, head of OMB's Office of Federal Procurement Policy, in an interview with *Government Executive*."

[4] Deloitte, *Calling a Change in the Outsourcing Market: The Realities for the World's Largest Organizations* (April 2005): "Organizations have now begun to recognize the real costs and inherent risks of outsourcing. Instead of simplifying operations, outsourcing often introduces complexity, increased costs, and friction into the value chain, requiring more senior management attention and deeper management skills than anticipated. In addition, outsourcing has allowed organizations to transfer financial and operational risk to vendors, but organizations are discovering that their contracts will never fully protect them against customer damage and business losses caused by service disruption. Many have responded by bringing operations back in-house and by exploring alternatives to traditional outsourcing, such as the Transform-Operate-Transfer model."

Mildred Warner, *From Reinvention to Public Service: Local Government Privatization Trends 1992-2002* (April 2005). While the percentages of services performed by local governments that are provided by contractors and public sector employees have held constant, new contracting out has decreased dramatically, although not as dramatically as new contracting in has increased. In fact, the services most often contracted out are in many instances the services most often contracted in, suggesting that local governments are not reluctant to bring services back in-house when they are poorly performed by contractors—a marked contrast to federal practice where one poorly performing contractor is all too often replaced with yet another poorly-performing contractor.

[5] *GovExec.com*, "Tangled Lines of Business" (April 15, 2006).

[6] Release Notes for the Public Draft for Comment of the Migration Planning Guidance for the Financial Management Line of Business (May 22, 2006).

[7] *GovExec.com*, "OMB: Competition key to consolidating financial systems" (April 28, 2006): "The General Services Administration, which is the lead agency managing the financial management line of business, already has released those documents to 12 selected private sector companies. GSA invited some companies that had responded to an initial request for information on financial management OMB released in 2004 to submit preliminary comments on advance copies of the guidance. Some industry sources said the process amounts to circumvention of the public review and comment period. `The government is doing a pre-public comment period with a selected vendors,' said an industry vice president, on condition of anonymity."

[8] 68 *Fed. Reg.* 32,134-5 (May 29, 2003).

[9] *Ibid.*, at 32,317.

[10] See May 22, 2006, Guidance, Attachment, page 5, 2(d)(ii).

[11] GovExec.com, "Procurement Chief Weighs Changes to Job Competition Rules" (January 14, 2005): "Agencies generally used direct conversions for outsourcing fewer than 10 full-time positions. But OFPP didn't have a good grasp on how frequently agencies performed direct conversions, and couldn't make agencies prove they saved money through the practice, (former Office of Federal Procurement Policy Administrator Angela) Styles said. Concerns arose that agencies were breaking tasks performed by 50 or 60 people apart into smaller chunks so that they could complete direct conversions, she added."

[12] OMB Circular A-76, Attachment B, page B-8, paragraph D(3)(a)(3), "Tradeoff Source Selection Solicitations Provisions."

[13] See May 22, 2006, Guidance, Attachment, page 4, 2(b)(ii)(F), "Use of FAR policies and procedures."

[14] See FAR 15.101-1.

[15] See May 22, 2006, Guidance, Attachment, page 3, paragraph 2(b)(i).

[16] *GovExec.com*, "OMB directed U.S. Mint to reopen job competition" (June 10, 2005).

[17] *Federal Times*, "DLA employees barred from competing for jobs" (June 27, 2005).

[18] See May 22, 2006, Guidance, Attachment, page 5, 2(d)(i): "OMB will consider deviations by agencies that wish to consider alternative models. As one example, an agency may wish to consider a two-step competition. In the first step, the customer might identify the best federal service provider after comparing the incumbent non-SSC in-house provider to SSC's using the Circular's costing principles and a highly streamlined evaluation process. The best federal service provider would then compete with the private sector providers…"